

**REPORT OF THE  
ASSOCIATION FINANCIAL EXAMINATION OF  
OLD AMERICAN INSURANCE COMPANY**

**AS OF  
DECEMBER 31, 2002**



**STATE OF MISSOURI  
DEPARTMENT OF INSURANCE  
JEFFERSON CITY, MISSOURI**

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Kansas City, Missouri  
August 2, 2004

Honorable Alfred W. Gross, Commissioner  
Virginia Bureau of Insurance  
Chairman of Financial Condition (EX4) Subcommittee  
Southeastern Zone Secretary

Honorable Jorge Gomez, Commissioner  
Wisconsin Department of Insurance  
Midwestern Zone Secretary

Honorable Scott B. Lakin, Director  
Missouri Department of Insurance  
301 West High Street, Room 530  
Jefferson City, Missouri 65102-0690

Gentlemen:

In accordance with your financial examination warrant, a full scope financial examination has been made of the records, affairs and financial condition of

**Old American Insurance Company**

hereinafter referred to as such, as Old American, or as the Company. Its administrative office is located at 3520 Broadway, Kansas City, Missouri 64111, telephone number 816-753-7299. This examination began on October 1, 2003, and concluded on the above date.

## **SCOPE OF EXAMINATION**

### **Period Covered**

The prior full scope association financial examination of Old American was made as of December 31, 1999, and was conducted by examiners from the State of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC), with no other zones participating.

The current full scope association financial examination covered the period from January 1, 2000, through December 31, 2002, and was conducted by examiners from the State of Missouri, representing the Midwestern Zone of the NAIC, with no other zone participating.

This examination was conducted concurrently with the examinations of the parent company, Kansas City Life Insurance Company (Kansas City Life) and a subsidiary, Sunset Life Insurance Company of America (Sunset Life).

This examination also included the material transactions and/or events occurring subsequent to the examination date, which are noted in this report.

### **Procedures**

This examination was conducted using the guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Missouri Department of Insurance (MDI) and statutes of the State of Missouri prevailed.

The examiners reviewed the work of the Company's independent auditor, KPMG LLP, of Kansas City, Missouri, for its audit covering the period from January 1, 2002, through December

31, 2002. Due to differences in approach and timing of the work of the independent auditors, only minimal use was made of the work of the independent auditors.

### **Comments - Previous Examination**

Listed below are comments, recommendations and notes of the previous examination report dated as of December 31, 1999, and the subsequent response or action taken by the Company.

#### **Board of Directors (page 5)**

*Comment:* The Company was directed to appoint twelve directors to its Board of Directors to be in compliance with its Bylaws or the Bylaws should be amended to allow for a smaller number of directors.

*Company's Response:* The Company did not formally respond to this comment.

*Current Findings:* The Company has not corrected this problem. See the Management section of this report for more details.

#### **Insolvency Clause**

*Comment:* The Company was directed to ensure that all existing and future reinsurance agreements contain insolvency clauses in compliance with Missouri Regulation 20 CSR 200-2.100(11) (Credit for Reinsurance)

*Company's Response:* The Company did not formally respond to this comment.

*Current Findings:* No additional problems were noted during the examination.

#### **Reinsurance Agreements**

*Comment:* The Company was directed to comply with the provisions of Missouri Regulation 20 CSR 200-2.300(4) (Life Reinsurance Agreements), which requires a ceding insurer to file with the MDI, any reinsurance agreement that involves the reinsurance of business prior to the effective date of the agreement. The Company's UNUM Life agreement was affected by the cited regulation.

*Company's Response:* The Company did not formally respond to this comment.

*Current Findings:* No additional problems were noted during the examination.

## **LIHTC Partnerships**

*Comment:* It was noted that the statement values reported by Old American for its LIHTC partnership investments were not based upon the GAAP equity method prescribed by the Accounting Practices and Procedures Manual of the NAIC. It was also noted that the Company had adopted an alternative reporting method. The Company was ordered to submit a written request to the MDI for specific approval if it wishes to admit statement values calculated from an alternative methodology.

*Company's Response:* The Company did not formally respond to this comment.

*Current Findings:* The Company has corrected the reporting problems indicated in a majority of the individual investments. However, continuing reporting problems were noted during this examination on a few immaterial cases. These have been included in separate communication to the Company.

## **Suspense Accounts**

*Comment:* The Company could not provide reconciliations, as of December 31, 1999, for most of the 19 suspense accounts included in the Remittances and Items Not Allocated line. The Company should ensure that all suspense accounts are reconciled on at least on a quarterly basis.

*Company's Response:* The Company did not formally respond to this comment.

*Current Findings:* Additional problems were noted regarding this account during this examination. See the Notes to the Financial Statements section of this report under "Remittances and Items Not Allocated" for more details.

## **HISTORY**

### **General**

Old American Insurance Company was founded by members of Thomas McGee & Sons, a Kansas City based insurance agency. The Company was incorporated on December 11, 1939, and commenced business on December 30, 1939, under the laws of the State of Missouri. The Company currently operates as a stock life insurance company, in accordance with the provisions of Chapter 376, Revised Statutes of Missouri (RSMo) (Life and Accident Insurance).

On November 25, 1986, the Company was purchased by C.S.B.I. Corp., an indirect wholly owned subsidiary of CenTrust Savings Bank, which was a Florida state chartered savings and loan association.

In November 1991, Kansas City Life purchased 100% of the stock of Old American and its subsidiaries, Missouri American Insurance Company and Old American Service Corporation. Subsequently, Missouri American Insurance Company was merged into Old American and Old American Service Corporation was dissolved in December 1992.

### **Capital Stock**

The Company is authorized to issue 800,000 shares of \$5.00 par value stock, which is separated into 192,630 shares of Class A preferred stock and 303,685 shares of Class B common nonvoting stock and 303,685 shares of common voting stock. As of December 31, 2002, 172,346 shares of Class A, preferred stock, 303,685 shares of Class B, common nonvoting stock and 299,437 shares of common voting stock were outstanding, resulting in total par values of \$963,150 for the Class A preferred stock and \$3,036,850 for the combined voting and nonvoting



common stock. Treasury stock consisted of 20,284 shares of Class A preferred stock and 4,248 shares of Class B common stock valued at \$101,420 and \$133,446, respectively.

### **Dividends**

Dividends were declared and paid in the amount of \$8,700,000 and \$5,625,000 for the years 2002 and 2001, respectively. Subsequent to the examination date, the Company paid an extra-ordinary dividend of \$22.3 million. This action was approved by the Missouri Department of Insurance in accordance with the applicable regulation.

### **Management**

The Bylaws require twelve (12) directors to be appointed to the Board. For the period under examination there was only ten (10) directors. Two vacancies have not been filled since the prior examination of the Company. The Company should staff twelve (12) directors on the Board to be in compliance with its Bylaws or the Bylaws should be amended to allow for a smaller number of directors.

The Board of Directors elected and serving as of December 31, 2002, were as follows:

<u>Name</u>	<u>Address</u>	<u>Principal Occupation and Business Affiliation</u>
Joseph R. Bixby	Kansas City, Missouri	Chairman of the Board, Kansas City Life
R. Philip Bixby	Kansas City, Missouri	President, CEO & Vice Chairman of the Board, Kansas City Life
Walter E. Bixby	Kansas City, Missouri	President, Old American
Charles R. Duffy, Jr.	Leawood, Kansas	Senior Vice President, Kansas City Life
Andrew M. Hansen	Kansas City, Missouri	Executive Vice President, Old American
Gary K. Hoffman	Kansas City, Missouri	Vice President, Associate General Counsel and Secretary, Old American
James J. Holmes	Kansas City, Missouri	Vice President, Old American
Tracy W. Knapp	Overland Park, Kansas	Senior Vice President, Kansas City Life
John K. Koetting*	Overland Park, Kansas	Vice President and Controller, Kansas City Life
Mark A. Milton	Leawood, Kansas	Senior Vice President, Kansas City Life

\*Resigned in January 2003 and was replaced by Robert J. Milroy effective April 2003.

The Company's Bylaws authorize an Executive Committee and any other committees that may be needed. The established committees and the members elected and serving as of December 31, 2002, were as follows:

Executive Committee

Joseph R. Bixby  
R. Philip Bixby  
Walter E. Bixby  
Gary K. Hoffman  
Tracy W. Knapp

Nominating and  
Compensation Committee

Joseph R. Bixby  
R. Philip Bixby  
Walter E. Bixby  
Gary K. Hoffman  
Tracy W. Knapp

Retirement Committee

John K. Koetting#  
Robert C. Miller

#Resigned and was replaced by John A. Showalter.

The senior officers elected and serving as of December 31, 2002, were as follows:

Joseph R. Bixby  
Walter E. Bixby  
Andrew M. Hansen  
Gary K. Hoffman  
James J. Holmes  
Robert E. Janes@  
Mary McCalla  
Robert J. Milroy

Chairman of the Board  
President  
Executive Vice President  
Vice President and Secretary  
Vice President – National Sales Manager  
Vice President and Controller  
Treasurer  
Vice President - Policy Administration

@Resigned December 2003 and was replaced by Brent C. Nelson effective January 2004.

**Conflict of Interest**

The Company requires its directors and officers to annually complete a conflict of interest questionnaire. Completed questionnaires were reviewed for all directors and officers for the examination period. No material conflicts were noted.

**Corporate Records**

The Company's Articles of Incorporation and Bylaws were reviewed for the period under examination. The Articles of Incorporation were not amended during the examination period. The Bylaws were amended on July 25, 2001, to change the day of the shareholders annual meeting from the Friday immediately preceding the fourth Monday in January to Thursday.

The minutes of the Board of Directors' meetings, committee meetings, and sole shareholder meetings were reviewed for proper approval of corporate transactions. In general, the minutes appear to properly reflect and approve the Company's major transactions and events for the period under examination.

**Acquisitions, Mergers and Major Corporate Events**

None

**Surplus Debentures**

No surplus debentures were issued or outstanding for the period under examination.

## **AFFILIATED COMPANIES**

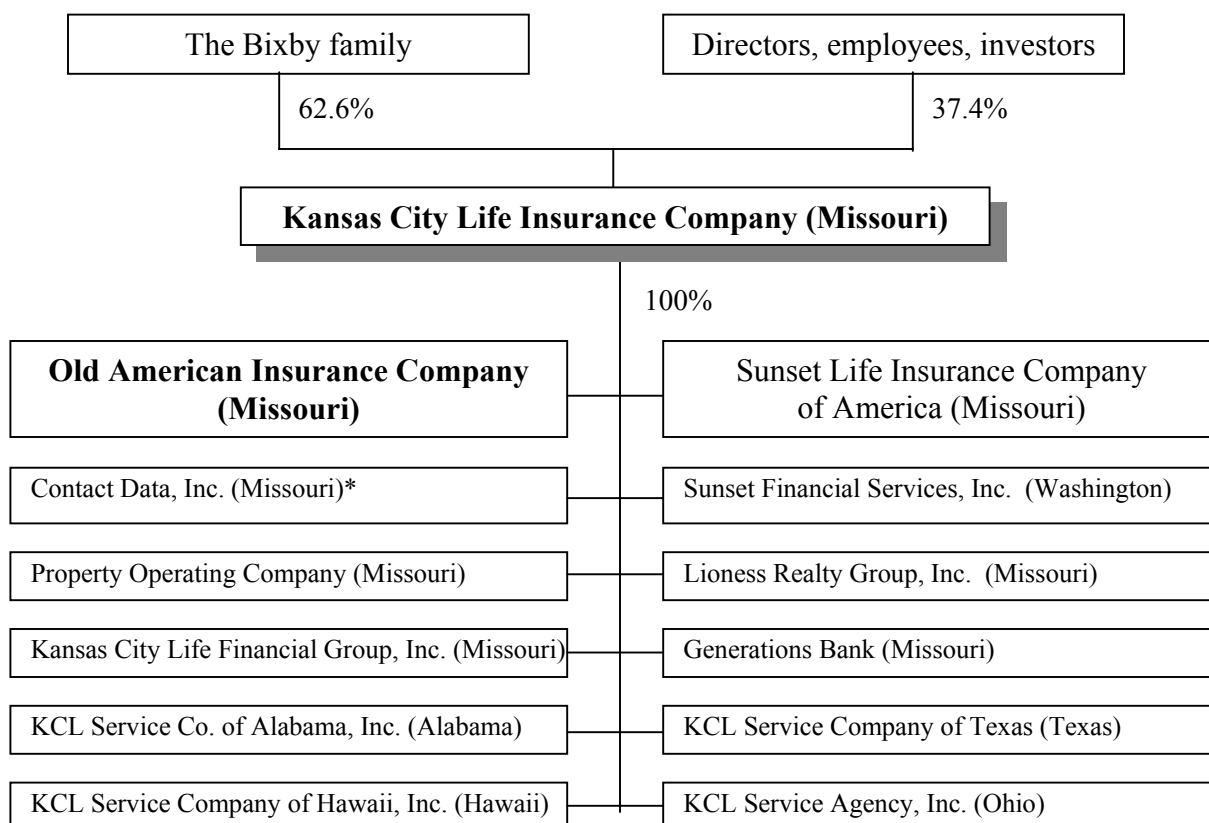
### **Holding Company, Subsidiaries and Affiliates**

The Company is a member of an Insurance Holding Company System as defined by Section 382.010, RSMo (Definitions). An Insurance Holding Company System Registration Statement was filed by the parent, Kansas City Life, for each year of the examination period on behalf of itself and its subsidiaries, including Old American. Old American is a wholly owned subsidiary of Kansas City Life. The Bixby family, consisting of several individuals, is the ultimate controlling entity of Kansas City Life.

The parent, Kansas City Life, is a life and health insurer organized as a Missouri corporation. The holding company system includes another life and health insurer, Sunset Life, and ten other affiliates that are related in part or entirely to the insurance operations. Contact Data, Inc., a Missouri corporation, works primarily for Old American by producing direct mailings and magazine inserts to generate new business leads. Sunset Financial Services, Inc. (SFS), a Missouri corporation, markets all of Kansas City Life and Sunset Life variable products and performs investment services for policyholders. Generations Bank, a federal stock savings bank chartered in Missouri, administers personal growth accounts (PGA) for Kansas City Life and its insurance subsidiaries' policyholders. Proceeds from claims and surrenders are deposited into a checking account with Generations Bank instead of paying the proceeds directly to the policyholder. The policyholder then becomes a customer of Generations Bank. Generations Bank also provides typical banking services to customers unrelated to the insurance operations. Lioness Realty Group, Inc. (Lioness) formerly managed the real estate owned by Kansas City Life and other non-affiliated companies, but is now inactive. The other six subsidiaries are currently inactive or do not have any significant operations.

## **Organizational Chart**

The following organizational chart depicts Old American's ownership and holding company structure, as of December 31, 2002:



\* Contact Data, Inc. terminated its corporate charter with the state of Missouri effective December 19, 2003.

## **Intercompany Transactions**

The Company's intercompany agreements are outlined below.

**1. Type:** Tax Allocation Agreement

**Affiliates:** Kansas City Life and Sunset Life

**Effective:** January 1, 1988

**Terms:** A consolidated federal income tax return is filed each year by Kansas City Life. The portion of the consolidated tax liability that is allocated to Old American and Sunset Life is based upon the subsidiary's liability on a stand-alone basis.

Intercompany tax settlements are made approximately 30 days after the filing of the tax return.

**2. Type:** Cost Sharing Agreement

**Affiliate:** Kansas City Life

**Effective:** May 22, 1992

**Terms:** Kansas City Life employees perform necessary services for Old American. These services include data processing, personnel, investment, tax, management, and other administrative services. Salaries and benefits are allocated based upon a time study for the applicable employees. Any expenses that are specifically for Old American are not subject to allocation and are charged 100% to Old American. Allocated costs are to be reimbursed at least on a quarterly basis.

**3. Type:** Loan Guarantee

**Affiliate:** Kansas City Life Insurance Company

**Effective:** August 4, 1999

**Terms:** Kansas City Life has guaranteed the indebtedness of Old American on borrowings under the Commerce Bank \$20,000,000 Line of Credit.

The amounts (paid) to and received from parent during the period under examination under the above agreements were as follows:

	<u>2000</u>	<u>2001</u>	<u>2002</u>
Cost Sharing Agreement – Old American:			
Paid to Kansas City Life	(\$4,062,000)	(\$3,907,000)	(\$3,288,000)
Dividend Payments:			
Paid to Kansas City Life	0	(5,625,000)	(8,700,000)
Federal Income Tax Allocation Agreement:			
(Paid to)/Received from – Kansas City Life	(2,455,578)	(1,553,993)	(3,600,368)
<b>Net Amount (Paid) or Received</b>	<b><u>(\$6,517,578)</u></b>	<b><u>(\$11,085,993)</u></b>	<b><u>(\$15,588,368)</u></b>

Kansas City Life has an account with State Street Bank for payment of claims for itself and its insurance subsidiaries, including Old American for the personal growth account business. The effect of this intercompany transaction was not properly reported in the Annual Statements of both companies. See notes 1 and 2 on the Notes to the Financial Statements section of this report for additional details.

### **FIDELITY BOND AND OTHER INSURANCE**

The Company is a named insured along with Kansas City Life and other affiliates on a financial institution bond with a liability limit of \$5,000,000 and a \$100,000 deductible. This coverage complies with the suggested minimum amount of fidelity insurance according to NAIC guidelines. Old American is also a named insured on additional insurance policies that include, but are not limited to, the following: commercial general liability, commercial property, workers compensation, commercial umbrella, directors and officers liability, and business automobile.

### **PENSION, STOCK OWNERSHIP AND INSURANCE PLANS**

Old American has employees for the customer service, sales and marketing, new business, claims, and legal functions. Other administrative functions of Old American's operations are performed by the employees of the parent, Kansas City Life. The Company is allocated a percentage of the benefit costs for Kansas City Life employees, pursuant to a Cost Sharing Agreement.

A variety of standard benefits are provided to the Company's employees and to Kansas City Life employees. These benefits include, but are not limited to, health insurance, dental insurance, life insurance, a defined benefit pension plan, and a 401(k) savings and profit sharing plan. Post-retirement health insurance is provided to retirees that meet eligibility requirements. The Company appears to have properly accounted for its direct and allocated employee benefits in the financial statements.

## STATUTORY DEPOSITS

### **Deposits with the State of Missouri**

The funds on deposit with the Missouri Department of Insurance as of December 31, 2002, as reflected below, were sufficient to meet the capital deposit requirements for the State of Missouri in accordance with Section 376.290 RSMo (Trust Deposits). The Company's required deposit for Missouri was \$600,000. The funds on deposit as of December 31, 2002, were:

<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
U.S. Treasury Notes	\$2,000,000	\$2,236,875	\$2,001,355

### **Deposits with Other States**

The Company also has funds on deposit with other states in which it is licensed. Those funds on deposit as of December 31, 2002, were:

<u>State</u>	<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
Georgia	U.S. Treasury Notes	\$100,000	\$110,188	\$97,358
Massachusetts	U.S. Treasury Notes	100,000	100,344	98,906
New Mexico	U.S. Treasury Notes	125,000	138,633	128,695
North Carolina	U.S. Treasury Notes	125,000	138,750	124,082
South Carolina	U.S. Treasury Notes	<u>1,300,000</u>	<u>1,453,969</u>	<u>1,300,881</u>
<b>Total</b>		<u>\$1,750,000</u>	<u>\$1,941,884</u>	<u>\$1,749,922</u>

### **Other Deposits**

The Company also had pledged assets to the Federal Home Loan Bank as collateral for \$25,000,000 of loans outstanding at the end of 2002. The pledged assets on deposit as of December 31, 2002, were:

<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
Bonds	\$28,710,786	\$28,093,369	\$28,093,369



The assets pledged as collateral to the Federal Home Loan Bank were not disclosed on Schedule E - Part 2 (Special Deposits) in the 2002 Annual Statement. The NAIC Annual Statement Instructions require disclosure of assets pledged assets since these assets are not for the benefit of all policyholders, claimants, and creditors of the Company. The Company should ensure that pledged assets are properly listed on Schedule E – Part 2 in the future.

In addition, the value of the Company's investment in Federal Home Loan Bank in the form of common stock, which is a required qualification for borrowing, was also pledged. Per NAIC Annual Statement Instructions, the Company should have reported the value of this stock on Schedule E – Part 2 of the Annual Statement. The Company should ensure that this arrangement is properly reported in the future.

## **INSURANCE PRODUCTS AND RELATED PRACTICES**

### **Territory and Plan of Operation**

Old American Insurance Company is licensed by the Missouri Department of Insurance under Chapter 376 RSMo (Life, Health and Accident Insurance). As of December 31, 2002, the Company was licensed to transact the business of insurance in 46 states and the District of Columbia. As of December 31, 2002, the Company had no pending licenses.

The Company primary products are “final expense” policies to pay for funeral and burial expenses and income replacement policies. These life products are marketed toward the senior citizen market. The individual life business accounted for 95% of total direct written premiums in 2002. An accident and health product, “Home Health Care,” is currently sold on a renewal basis only and no new policies have been issued since 1993.

Old American sells its products mainly through agents who rely on leads generated from direct mail solicitation, television advertising, and telemarketing. The Company utilizes approximately 50 agencies located throughout the United States to sell its products.

The parent, Kansas City Life, has an internal audit staff that performs agency audits.

**Policy Forms & Underwriting**  
**Advertising & Sales Materials**  
**Treatment of Policyholders**

The Missouri Department of Insurance has a market conduct staff that performs a review of these issues and generates a separate market conduct report. The market conduct staff is currently performing a limited scope of the Company's rate books and underwriting manuals for the period spanning the Company's start of business through December 31, 1980. As of the end of this examination fieldwork, the report of the limited scope market conduct examination is not ready for our review and analysis.

The California Department of Insurance performed a market conduct examination of the Company's claims practices and procedures in California for the period February 1, 2001 through March 31, 2002 (report dated November 19, 2002). Minor errors were noted in the report and addressed by Company management. These do not appear to affect the Company's financial position.

**REINSURANCE****General**

The Company's premium and annuity activity on a direct written, assumed and ceded basis, for the period under examination, is detailed below:

	<b><u>2002</u></b>	<b><u>2001</u></b>	<b><u>2000</u></b>
Direct Business	\$77,585,444	\$80,353,323	\$83,783,368
Reinsurance Assumed			
None	0	0	0
Reinsurance Ceded:			
Affiliates	0	0	0
Non-affiliates	<u>(7,369,540)</u>	<u>(8,471,186)</u>	<u>(9,688,898)</u>
<b>Net Premiums Written</b>	<b><u>\$70,215,904</u></b>	<b><u>\$71,882,137</u></b>	<b><u>\$74,094,470</u></b>

**Assumed**

The Company does not assume any business.

**Ceded**

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that an assuming reinsurer fails to perform its obligations under the reinsurance agreement.

Old American's only significant agreement for ceded life business is a coinsurance agreement with Employers Reassurance Corporation, effective December 1, 1989. This agreement cedes 100% of the risks for certain whole life policies issued prior to December 1, 1986. As of December 31, 2002, the ceded insurance in-force and ceded reserves for this agreement were \$85,504,025 and \$ 39,181,468 respectively, representing 99% of both totals.

The Company has two significant reinsurance agreements for Accident and Health business that pertain to the Home Health Care Product. There have not been any new Home

Health Care policies sold since 1993 and the remaining business represents renewals. An agreement with GE Reinsurance Corporation effective January 1, 1989, cedes 50% of the benefits payable for the Home Health Care policies. An agreement was executed with UNUM Life Insurance Company of America (UNUM Life), effective October 1, 1998, to cede the remaining 50% of the liabilities for these policies. As of December 31, 2002, the total reserves ceded on this business were \$24,709,683.

## **ACCOUNTS AND RECORDS**

### **General**

The Company's financial statements were audited by the CPA firm, KPMG, LLP, of Kansas City, Missouri, for all years in the examination period.

Policy and claim reserves were reviewed and certified by Stephen A. Bader, FSA, MAAA, for all years in the examination period. Mr. Bader is an employee of Kansas City Life.

The Company's accounting system with respect to its general ledger and the trial balances is unusually complex resulting in numerous non-ledger entries that do not reconcile to the related lines of the Annual Statement. As a result of these numerous non-ledger accounts, it is necessary that the Company prepare and maintain a reconciliation of statutory capital and surplus with the ledger capital and surplus accounts, including the non-ledger items. It is also necessary that the Company's non-ledger entries indicate which line of the Annual Statement (pages 2 through 4) the entry relates, to provide for ease of tracing amounts from the general ledger and the related non-ledger accounts to the affected Annual Statement lines. As an alternative, the Company may choose to eliminate the non-ledger system and replace it with a

system that assigns general ledger account numbers to accounts, as is customary in the insurance industry.

The Company's custodial agreement with United Missouri Bank that was in effect during the examination period was deficient relative to the requirements of the NAIC, as stipulated in the Financial Examiners Handbook. Kansas City Life provided a revised and an updated version of the agreement; however, the agreement was also deficient, as it did **not** contain an acknowledgment by the custodian to assume liability for consequential damage that may arise out of loss or theft of the securities under custody. This language is contained in section 6(a) of the custodial agreement. The Company is directed to amend the agreement to include the specific language. Also, the Company could not provide a custodial agreement regarding securities on custody with Fidelity Investments Company. The Company is directed to obtain custodial agreement from Fidelity Investments Company and ensure that the agreement wordings reflect in its entirety the requirements of the NAIC with respect to custodial agreements.

## **FINANCIAL STATEMENTS**

The following financial statements, with supporting exhibits, present the financial condition of Old American for the period ending December 31, 2002. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Notes to the Financial Statements." The failure of any column of numbers to add to its respective total is due to rounding or truncation.

There may have been additional differences found in the course of this examination, which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial concerning their effect on the financial statements, and therefore

were only communicated to the Company and noted in the workpapers for each individual Annual Statement item.

## Assets

	Ledger Assets	Assets Not Admitted	Net Admitted Assets
Bonds	\$161,560,236	\$2,007,559	\$159,552,677
Preferred Stocks	1,740,519		1,740,519
Common Stocks	1,250,000		1,250,000
Mortgage Loans on Real Estate	45,788,305		45,788,305
Policy Loans	7,297,322		7,297,322
Cash and Short-term Investments (Note 1)	36,779,086	(3,489,883)	40,268,969
Other Invested Assets	4,785,625	1,491,449	3,294,176
Amounts Recoverable from Reinsurers	1,059,013		1,059,013
Electronic Data Processing Equipment	87,093		87,093
Federal Income Tax Recoverable	21,071,371	18,302,449	2,768,922
Guaranty Funds Receivable	59,029	25,094	33,935
Life Insurance Premiums and Annuity Consideration Deferred and Uncollected	17,196,022	15,643	17,180,379
Accident and Health Premiums Due and Unpaid	22,146	206	21,940
Receivable from Parent, Subsidiaries and Affiliates (Note 2)	(14,044)	14,044	0
Investment Income Due and Accrued	2,956,672	99,466	2,857,206
Amounts Due from Agents	586,384	586,384	0
Other Assets Non-Admitted	68,974	68,974	0
<b>TOTAL ASSETS</b>	<b><u>\$302,293,753</u></b>	<b><u>\$19,121,385</u></b>	<b><u>\$283,200,456</u></b>

## Liabilities, Surplus and Other Funds

Aggregate Reserve for Life Policies and Contracts	\$193,969,291
Aggregate Reserve for Accident and Health Policies	1,152,601
Liability for Deposit-type Contracts	123,977
Policy and Contract Claims – Life	7,107,353
Policy and Contract Claims – Accident and Health	610,344
Premiums and Annuity Considerations Received in Advance	338,443
Interest Maintenance Reserve	848,033
General Expenses Due or Accrued	1,821,848
Taxes, Licenses and Fees Due or Accrued	500,000
Federal Income Taxes	2,116,681
Unearned Investment Income	331,758
Amounts Withheld or Retained	4,644,665
Amounts Held for Agents' Account	89,149
Remittances and Items Not Allocated ( <b>Note 3</b> )	691,518
Borrowed Money	25,033,375
Asset Valuation Reserve	1,700,000
Payable to Parent, Subsidiaries and Affiliates ( <b>Note 2</b> )	3,578,287
Aggregate Write-Ins for Liabilities:	
Funds Due Under Reinsurance Treaties in Authorized Companies	298,000
Reserve for Additional Expense on Reinsurance Ceded	<u>409,826</u>
<b>TOTAL LIABILITIES</b>	<b>\$245,365,149</b>
Common Capital Stock	3,036,850
Preferred Capital Stock	963,150
Gross Paid In and Contributed Surplus	93,920
Unassigned Funds (Surplus)	33,976,253
Less Treasury Stock:	
Common Stock	(133,446)
Preferred Stock	<u>(101,420)</u>
Capital and Surplus	<b><u>\$37,835,307</u></b>
<b>TOTAL LIABILITIES AND SURPLUS</b>	<b><u>\$283,200,456</u></b>

## Summary of Operations

Premiums and Annuity Considerations	\$70,215,904
Net Investment Income	16,159,947
Amortization of Interest Maintenance Reserve	149,684
Commission and Expense Allowances on Reinsurance Ceded	1,040,839
Miscellaneous Income	<u>(236,476)</u>
<b>TOTAL</b>	<b>\$87,329,898</b>
Death Benefits	41,553,586
Matured Endowments	32,412
Disability Benefits and Benefits Under Accident & Health Policies	704,138
Surrender Benefits and Withdrawals for Life Contracts	4,002,232
Interest and Adjustments on Contract and Deposit-type Contract Funds	4,977
Payments on Supplementary Contracts with Life Contingencies	9,747
Increase in Aggregate Reserves for Life and Accident & Health Policies	4,858,065
Commissions on Premiums and Annuity Considerations	12,485,421
General Insurance Expenses	11,762,424
Insurance Taxes, Licenses and Fees	1,788,149
Increase in Loading on Deferred and Uncollected Premiums	<u>(204,769)</u>
<b>TOTAL</b>	<b><u>\$76,996,382</u></b>
<b>NET GAIN FROM OPERATIONS</b>	<b>\$10,333,516</b>
Federal Income Taxes Incurred	3,291,214
Net Realized Capital Gains and Losses	<u>(1,629,223)</u>
<b>NET INCOME</b>	<b><u>\$5,413,079</u></b>



## **Capital and Surplus Account**

Capital and Surplus, December 31, 2001	\$41,244,801
Net Income	5,413,079
Change in Net Unrealized Capital Gains or (Losses)	(2,562,739)
Change in Non-Admitted Assets	(944,290)
Change in Asset Valuation Reserve	1,650,000
Change in Net Deferred Income Tax	1,734,456
Dividends to Stockholders	<u>(8,700,000)</u>
<b>Net Change in Capital and Surplus</b>	<b><u>(\$3,409,494)</u></b>
 <b>CAPITAL AND SURPLUS, DECEMBER 31, 2002</b>	 <b><u>\$37,835,307</u></b>

## **Notes to the Financial Statements**

### **Note 1 – Cash and Short-term Investment \$40,268,969**

The amount reported by the Company for this account was increased by \$3,564,243 and the amount reported by the Company for Payable to Parent, Subsidiaries and Affiliates was increased by the same amount. This reclassification was made to properly reflect the Company's transaction with Kansas City Life with respect to the personal growth account business. Kansas City Life has an account with State Street Bank for payment of claims for itself and its insurance subsidiaries, including Old American for the personal growth account business. The account, according to Kansas City Life, is utilized to pay claims for each of the subsidiaries and the subsidiaries are required to reimburse Kansas City Life. In effect, this is a joint intercompany claims account, for which Kansas City Life is the paymaster. As of December 31, 2002, Old American improperly included \$3,564,243 owed to Kansas City Life as part of its cash account as a negative balance with State Street bank. However, this examination was unable to confirm

this amount with State Street Bank, as the amount does not reside with the bank. This balance actually represents an intercompany transaction payable, which should have been reported differently as part of related party transactions. The Company is directed to report as its cash only those amounts that actually reside with the bank and can be verified through direct confirmation by the examination process.

<b>Note 2 - Payable to Parent, Subsidiaries and Affiliates</b>	<b>\$3,578,287</b>
<b>Receivable from Parent, Subsidiaries and Affiliates</b>	<b>\$0</b>

The amount reported by the Company for this account was increased by a combination of \$3,564,243 to reflect intercompany transactions improperly reported by the Company as part of the Cash account, see Note #1 above and a reclassification of \$14,044 negative balance improperly reported as Receivable from Parent, Subsidiaries and Affiliates line of the Annual Statement. The Company is directed to properly and accurately report the arrangement with Kansas City Life with respect to payment of claims arising from the personal growth account in the future. The Company should also ensure that final account balance resulting from related party transactions are properly classified (receivable or payable) on the Annual Statement.

In addition, the underlying transaction between Kansas City Life and the Company with respect to the payment of claims arising from the personal growth account constitutes an intercompany transaction in accordance with the Missouri holding company law. Consequently, the Company is directed to enter into an intercompany agreement with Kansas City Life, describing each entity's role with respect to the payment of claims in the personal growth account. The Company should submit the agreement to the MDI in accordance with Section 382.195 RSMo (Transactions within a holding company system).

**Note 3 – Remittances and Items Not Allocated****\$691,518**

As noted in the prior examination, the Company continues to have reporting problems regarding transactions in this account. The problems can be summarized as follows: 1) most of the general ledger accounts included in the Annual Statement balance included both debits and credits, which were netted and included as a single amount for Annual Statement purposes. Per SSAP #64 (Offsetting and Netting of Assets and Liabilities) only debits and credits for the same party may be offset - the Company cannot offset a liability to one policyholder with an asset due from a different policyholder. Any debit balances should be shown on the Asset page of the Annual Statement (on the appropriate line) and a determination of admissibility made based on SSAP #4 (Assets and Nonadmitted Assets) and 2), several of the general ledger accounts with credit balances did not meet the criteria for reporting on this line of the Annual Statement. Per the NAIC Annual Statement instructions, this line should include "cash receipts that cannot be identified for a specific purpose or, for other reasons, cannot be applied to a specific account when received". The Company included claims payment liabilities, reinsurance liabilities, garnishments, etc., which clearly do not meet the above definition. The Company should ensure that, per SSAP #64, unrelated debits and credits within the same general ledger account or between two or more general ledger accounts are not netted, but included as distinct assets/liabilities on the Annual Statement. In addition, the Company should ensure it follows the NAIC SSAP's and Annual Statement Instructions guidance in completing the Annual Statement.

## **Examination Changes**

--None--

## **General Comments and/or Recommendations**

### **Board of Directors (page 6)**

The Company should staff twelve directors on the Board of Directors to be in compliance with its Bylaws or the Bylaws should be amended to allow for a smaller number of directors.

### **Other Deposits (page 13)**

The Company should ensure that its assets pledged as collateral to the Federal Home Loan Bank, including the pledged value of the common stock of Federal Home Loan Bank owned by the Company are properly disclosed on Schedule E – Part 2 (Special Deposits) of the Annual Statement in the future.

### **Accounts and Records (page 17)**

The Company should reduce and possibly eliminate the unusual complexity in its accounting system by abandoning the non-ledger approach and replacing the current system with one that assigns general ledger numbers to accounts that can easily be traced to the Annual Statement lines. Alternatively, the Company should prepare and maintain reconciliation workpapers for Annual Statement lines on pages 2 through 4 of the Annual Statement.

### **Custodial Agreements (page 18)**

The Company's custodial agreement with United Missouri Bank is deficient, as it did **not** contain an acknowledgment by the custodian to assume liability for consequential damage that may arise out of loss or theft of the securities under custody.

The Company could not provide a custodial agreement regarding securities on custody with Fidelity Investments. The Company is directed to obtain custodial agreement from Fidelity Investments Company and ensure that the agreement wording reflect in its entirety the requirements of the NAIC with respect to custodial agreements.

### **Cash and Short-term Investments (page 22)**

The Company improperly reported payables to Kansas City Life originating from related party transactions as part of the cash account. The Company is directed to report as cash only those amounts that actually reside with the bank and can be verified through direct confirmation by the examination process.

### **Payable/Receivable to/from Parent, Subsidiaries and Affiliates (page 23)**

Kansas City Life has an account with State Street Bank for payment of claims for itself and its insurance subsidiaries, including Old American for the personal growth account business.

At year-end 2002, Old American owed Kansas City Life for unreimbursed claims paid on its behalf by Kansas City Life. However, Old American improperly reported the unreimbursed amount as part of cash, which understated the amount payable to its parent. The Company is directed to properly and accurately report the underlying transaction in the future.

The Company improperly reported net payables from related party transactions on the intercompany receivable line of the Annual Statement. The Company should ensure that the

final account balance resulting from related party transactions are properly classified (receivable or payable) on the Annual Statement.

The underlying transaction between Kansas City Life and Old American as noted above constitutes an intercompany transaction in accordance with the Missouri holding company law. The Company should submit an agreement to the MDI in accordance with Section 382.195 RSMo (Transactions within a holding company system) for review and possible approval.

**Remittances and Items Not Allocated (page 24)**

The Company's accounting and reporting for this line of the Annual Statement is inconsistent with prescribed standards and procedures. The Company should ensure that, per SSAP #64, unrelated debits and credits within the same general ledger account or between two or more general ledger accounts are not netted, but included as distinct assets/liabilities on the Annual Statement. Overall, the Company should ensure it follows NAIC SSAP's and NAIC's Annual Statement Instructions guidance in completing the Annual Statement.

### ACKNOWLEDGMENT

The assistance and cooperation extended by the officers and the employees of Old American Insurance Company during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Bernie Troop, CFE, Shawn Hernandez, CFE, Karen Baldree, AFE, and Barbara Bartlett, AFE, CPA, examiners for the Missouri Department of Insurance, also participated in this examination. Andrew Balas, CFE, AES, Computer Audit Specialist for the Missouri Department of Insurance performed a review of the information system environment. Timothy Harris, FSA, MAAA of Milliman USA, Inc., also participated as a consulting actuary.

### VERIFICATION

State of Missouri                    )  
  )  
County of                                )

I, Levi N. Nwasoria, CPA, CFE on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of the Company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

\_\_\_\_\_  
Levi N. Nwasoria, CPA, CFE  
Examiner-In-Charge  
Missouri Department of Insurance

Sworn to and subscribed before me this \_\_\_\_\_ day of \_\_\_\_\_, 2004.

My commission expires: \_\_\_\_\_  
\_\_\_\_\_  
Notary Public

### SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

\_\_\_\_\_  
Frederick G. Heese, CFE, CPA  
Audit Manager  
Missouri Department of Insurance